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Restructuring Practices in Norway

1. Introduction

Amidst the early phases of the COVID-19 pandemic in 2020, Norway introduced a new formal restructuring framework (*rekonstruksjonsforhandlinger*). In addition to mitigating the effects of the pandemic on the Norwegian economy, the purpose of the new framework was to enable the continuation of viable businesses despite the distress of the legal entity carrying on the business.[1] The new framework replaced a debt composition framework that was widely perceived as dysfunctional. While the new framework is set out in a temporary act that was initially intended to expire on 1 January 2022, the act's expiry date has repeatedly been postponed.[2]

The use of the new restructuring framework has been modest. Data sourced from the Brønnøysund Register Centre shows that 14 limited liability companies entered formal restructuring proceedings in 2023.[3] By comparison, 3,745 legal entities, almost all of which were limited liability

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1 Prop. 75 L (2019–2020) 12.

2 At the time of writing, the act is set to expire on 1 July 2025, see *rekonstruksjonsloven* § 64.

3 <https://w2.brreg.no/kunngjoring/kombisok.jsp?datoFra=01.01.2023&datoTil=31.12.2023&id_region=0&id_niva1=110&id_bransje1=0 > accessed 6 November 2024.

companies, entered insolvent winding-up proceedings (*konkurs*) during the same period.[4]

It is perhaps intuitive to regard the relatively low use of formal restructuring proceedings as a failure on the part of the Norwegian legislator; the low number of proceedings could be seen as evidence of the framework's shortcomings. Such criticism would likely reflect the view that low usage implies that Norwegian restructuring and insolvency law is failing to ensure that a company's distress does not cause the closure of viable businesses.[5] It is therefore reasonable to interpret misgivings over the low usage as reflecting the position that a larger number of viable businesses would have continued to operate if more companies had entered formal restructuring proceedings. If this view is correct, it is likely that, in recent years, there have been instances where viable Norwegian businesses have ceased to operate.

However, the low use of Norwegian restructuring proceedings is also compatible with another explanation: the management and shareholders of distressed companies with viable businesses may be using other means to ensure that their businesses continue to operate. They may do so by agreeing on a debt restructuring with their creditors through informal negotiations ('out-of-court restructuring'), thereby allowing the same company to continue its business. Moreover, asset sales from an insolvent company's estate to a solvent company could ensure the survival of the insolvent company's business despite the demise of the legal entity that previously carried out the operations.

The existence of several plausible explanations for the low use of formal restructuring proceedings raises the question of whether there is reason to believe that distressed companies with viable businesses rely on means other than formal restructuring to ensure their business continuity. This article

4 <www.ssb.no/virksomheter-foretak-og-regnskap/konkurser/statistikk/opna-konkursar/artikler/4-517-konkursar-i-2023> accessed 6 November 2024.

5 References to a 'company' should generally be understood as referring to a private limited liability company. The rules governing such companies are set out in *aksjeloven* [the Private Limited Liability Companies Act]. The rules governing public limited liability companies are set out in *allmennaksjeloven* [the Public Limited Liability Companies Act]. In many respects, the provisions of the two acts are identical, including in relation to all company law issues discussed in this article.

contributes to answering that question by identifying the circumstances under which it is preferable for those in control of a distressed company's decision-making to use alternatives to formal restructuring for securing the business's survival. The key findings are that a company seeking to restructure bond debts issued in the Norwegian market will often prefer an out-of-court restructuring over formal restructuring proceedings, and that an owner-manager of a distressed company may, in some cases, have reason to favour winding-up over formal restructuring proceedings.

2. Background

2.1. Overview of Norwegian corporate insolvency law

The fundamental pillar of Norwegian insolvency law is the *konkurs* proceeding. The commencement of a *konkurs* involves the creation of an insolvency estate that takes control of an insolvent debtor's assets,[6] sells them, and distributes the sale proceeds among the unsecured creditors in accordance with a statutorily defined hierarchy. Security interests over the debtor's assets generally survive the commencement of a *konkurs* and entitle the secured creditors to be paid out of the secured assets ahead of the insolvency estate.[7]

While most *konkurs* proceedings concern limited liability companies, both natural and legal persons may be subject to a *konkurs* proceeding.[8] When a company becomes subject to a *konkurs*, it effectively heralds that the company will cease to exist.[9] Since, for present purposes, we are concerned with insolvency proceedings applicable to limited liability companies, I will use the term 'insolvent winding-up proceedings' when referring to *konkurs* proceedings.

6 *Dekningsloven* [the Creditors' Recovery Act] § 2-2.

7 *Dekningsloven* § 8-14. However, a *konkurs* could render a security interest ineffective due to a failure to perfect the security prior to the proceedings or the security interest being liable to transaction avoidance.

8 Mads Henry Andenæs, *Konkurs* (M.H. Andenæs 2009) 77.

9 *Konkursloven* [the Insolvency Act] § 138.

Konkursloven § 117 instructs the insolvency professional managing the insolvency estate to sell the insolvent company's assets in the manner that is most likely, given the circumstances, to generate the largest amount of proceeds. Among other things, this means that the relevant legislation does not embody a preference for outcomes where a purchaser of the debtor's assets continues the debtor's business. When considering two competing bids for the debtor's assets, the insolvency professional is to choose the bid with the most favourable terms. On the other hand, there is nothing preventing a purchaser from continuing to carry on the business. Nor is there any prohibition on selling to a purchaser who was among the company's shareholders or management prior to the proceedings, although the main rule is that the insolvency professional must advertise the sale to the public before selling assets to such parties.[10]

These features of Norwegian insolvent winding-up proceedings enable the use of such proceedings for the purpose of restructuring a business. This process would involve the following steps: An owner-manager of an insolvent company uses his influence to ensure that the company petitions for the opening of the proceedings.[11] At the same time, the owner-manager establishes a new company and submits a bid for the insolvent company's assets. Assuming the bid is successful, the new company acquires the assets. Any security interests over the transferred assets will continue to subsist following the transfer. However, insofar as the value of the secured asset is insufficient to cover all secured creditors, the security interest will be modified to secure only the amount covered by the secured asset's value.[12]

Another avenue for restructuring a business is to initiate restructuring proceedings (*rekonstruksjonsforhandlinger*). I shall refer to such proceedings as 'formal restructuring proceedings.' The framework for formal restructuring proceedings is, as touched upon in Section 1, currently set out in a temporary act adopted by the Norwegian parliament in May 2020.[13]

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10 *Konkursloven* § 117, second paragraph.

11 See *aksjeloven* [the Private Limited Liability Companies Act] § 6-18.

12 *Konkursloven* § 117a.

13 The Norwegian government is working on a proposal for permanent legislation and has published draft legislation for consultation.

Of most importance for present purposes are the possibilities the current framework offers for restructuring debts. There are two tracks available for restructuring debts: *frivillig rekonstruksjon* (consensual restructuring) and *rekonstruksjon med tvangsakkord* (non-consensual restructuring). As a consensual restructuring requires the consent of all affected creditors, a non-consensual restructuring is the track of most practical use for a debtor.

A non-consensual restructuring may, among other things, consist of a writing down of debts, a postponement of maturities and/or the conversion of debts to shares.[14]

In principle, any claim arising out of circumstances existing prior to the opening of the restructuring proceedings is liable to be altered by a non-consensual restructuring.[15] However, by way of exception, certain claims cannot be affected by a non-consensual restructuring.[16] This means that such claims are not liable to be written down or otherwise altered without the consent of the creditor. These claims include secured claims (insofar as the value of the secured assets covers the secured claim), claims with preferential priority in an insolvent winding-up, and creditors with a right to set off their claims against debts owed to the company.

Following the company's presentation of a restructuring proposal, a single vote is held among the creditors.[17] This means that there is no formation of creditor classes. The adoption of a restructuring requires the consent of at least half of the creditors entitled to vote (as opposed to those actually voting). As a general rule, voting rights accrue to all creditors with claims against the company at the time the proceedings commenced.[18] By way of exception, some of these creditors do not have voting rights. This includes creditors whose claims are not liable to alteration (e.g., secured creditors) and persons closely connected to the company.

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14 *Rekonstruksjonsloven* [the Restructuring Act] § 34(1). It is, as a main rule, not possible to force creditors to become shareholders through a conversion of debts to shares, see *rekonstruksjonsloven* § 34(3).

15 *Rekonstruksjonsloven* § 54, first sentence.

16 *Rekonstruksjonsloven* § 54, second sentence.

17 *Rekonstruksjonsloven* § 42.

18 *Rekonstruksjonsloven* § 41.

As mentioned, a non-consensual restructuring can involve the conversion of debts into shares. Such a conversion requires the issuance of new shares and, therefore, necessitates an amendment to the company's articles of association. As a matter of company law, such amendments require the assent of a qualified majority of shareholders at the company's general meeting.[19] This requirement also applies in restructuring proceedings, but with the modification that approval from half of the shareholders suffices.[20]

2.2. **The companies entering winding-up proceedings**

As discussed, an important policy goal of the Norwegian formal restructuring proceedings is to save viable businesses. As touched upon in Section 1, a low ratio of formal restructuring proceedings to insolvent winding-up proceedings is not necessarily evidence of policy failure in this regard. For one, there is the possibility that the companies entering insolvent winding-up proceedings generally do not have viable businesses. As acknowledged by the Norwegian legislator, the cessation of such businesses does not conflict with the policy goal of saving viable businesses.[21]

This raises the question of what is known about the viability of the businesses of Norwegian companies entering insolvent winding-up proceedings. Norwegian policy documents do not explain the criteria for distinguishing viable businesses from their non-viable counterparts. It is useful, for present purposes, to consider a similar distinction from the financial economics literature, namely that between financial and economic distress. Financial distress denotes a situation where a company has insufficient cash flow to service its debt obligations.[22] By contrast, economic distress denotes a situation where the company's business model is not viable.[23] The difference between a company facing financial distress and one experiencing economic

19 *Aksjeloven* § 5-18.

20 *Rekonstruksjonsloven* § 35.

21 Prop. 75 L (2019–2020) 12.

22 Edward I Altman, Edith Hotchkiss and Wei Wang, *Corporate Financial Distress, Restructuring, and Bankruptcy: Analyze Leveraged Finance, Distressed Debt, and Bankruptcy* (4th edn, Wiley 2019) 8.

23 ibid.

distress thus concerns the ability of the company's business to generate positive operating income: a financially distressed company's business is capable of doing so, whereas an economically distressed company's business is not. This means that there is a debt threshold under which a financially distressed company will generate profits. Conversely, the business of an economically distressed company will be unable to generate a profit even if all its debt obligations are cancelled.

There is no data directly concerning the percentage of companies entering insolvent winding-up proceedings facing financial (as opposed to economic) distress. However, the annual accounts of such companies can provide some insight in this regard. An insolvent company's operating income in the year preceding the opening of insolvency proceedings is likely to offer some indication as to whether the company was suffering from financial or economic distress upon entering the proceedings. A positive operating income would suggest that the company was suffering from financial distress, whereas a negative operating income would suggest economic distress. Some caveats are necessary. Historical operating income does not necessarily indicate whether a company was financially or economically distressed at the time of entering insolvent winding-up proceedings. Moreover, there could be cases where a part of a company's business is profitable and thus viable, even if the combined income from all its business lines is negative. Therefore, the fact that a company recorded a negative operating income in the year preceding insolvent winding-up proceedings does not necessarily imply that the company was economically distressed when the proceedings commenced.

According to data downloaded from Proff Forvalt, 3,703 Norwegian private limited liability companies entered insolvent winding-up proceedings in 2023. For 1,256 of these companies, Proff Forvalt's database contains information about their operating income in 2022. In this sample, 307 of the 1,256 companies had a positive operating income in 2022. For most of these companies, the surplus was modest: only 31 companies had an operating income exceeding NOK 1 million (approx. EUR 84,000). Bearing in mind the aforementioned caveats, the low number of companies with positive operating income suggests that a large majority of the companies in the sample were likely economically distressed.

3. The restructuring decision

3.1. Introduction

The data presented in Section 2.2 provides some indication that many of the companies entering Norwegian insolvent winding-up proceedings are economically distressed and therefore do not have a viable business. It is not a policy failure that such companies do not commence formal restructuring proceedings.

The fact that many companies face distress of an economic nature does not preclude the existence of financially distressed companies that do not enter formal restructuring proceedings. In other words, it cannot be concluded that the companies entering formal restructuring proceedings are the only ones suffering from financial distress. Whether the fact that some financially distressed companies do not initiate formal restructuring proceedings conflicts with the goal of saving viable businesses depends on whether the businesses of such companies cease to operate despite being viable. The answer to this question, in turn, hinges on whether financially distressed companies successfully use other means to ensure the continuation of their businesses. Insofar as they do so, their decision not to initiate formal restructuring proceedings is not contrary to the policy goal of saving viable businesses.

To shed light on whether financially distressed companies resort to alternative means to preserve their businesses, the following section will consider the circumstances under which the board of a financially distressed Norwegian company would regard out-of-court restructuring or insolvent winding-up as preferable options for ensuring the survival of the business. The focus on the board's preferences is warranted because, under Norwegian company law, the board is responsible for deciding whether to initiate formal restructuring proceedings or insolvent winding-up proceedings on the company's behalf.[24]

It is necessary to make certain assumptions regarding the board's preferences. To simplify the analysis, attention will be restricted to cases where the choice between formal restructuring proceedings and alternative means

[24] *Aksjeloven* § 6-18.

is made by a single 'owner-manager', meaning a person who is both the sole board member and the sole shareholder of the company. It will further be assumed that this person acts with the aim of maximising their personal wealth.

Assuming that a company's distress is purely financial, it would be desirable to continue the company's business if it can be placed within a legal entity with a sustainable debt load. There are two primary means of achieving such an outcome. The first option is to reduce the company's debts to a level that its income is sufficient to service. In this case, the business continues within the same company, now relieved of its excessive debt load. The second option is to transfer the business to a different legal entity that is not facing financial distress. Both options share the common outcome of ensuring that the business is carried on within a legal entity unburdened by a debt load that is unproportionally high to the business' income.

The first option is most readily achieved through the original company restructuring its debts. This can be accomplished through out-of-court negotiations with creditors or through formal restructuring proceedings. The second option can be executed by placing the distressed company into insolvent winding-up proceedings, after which a newly formed company controlled by the owner-manager purchases from the insolvency estate the assets necessary to continue the business of the insolvent company.

3.2. **Out-of-court restructurings of bonds**

This subsection examines the advantages and disadvantages of formal restructuring proceedings compared to out-of-court debt restructuring. This analysis could offer a partial explanation for the low number of formal restructuring proceedings: some financially distressed companies may resolve their distress through out-of-court restructuring rather than resorting to formal proceedings.

When referring to 'out-of-court debt restructurings', I have in mind cases where a company and its creditors execute a debt restructuring by relying on contract law and, where applicable, company law if the company is to issue new shares. Under Norwegian law of obligations, any amendment to a debt obligation requires the consent of the creditor holding that

obligation.[25] This means that a company seeking to secure postponements of maturities, reductions in principal, or other amendments to a set of debt obligations must obtain the consent of all creditors concerned.

As discussed in Section 2.1, Norwegian formal restructuring proceedings provide the option of a non-consensual restructuring of unsecured debts. Compared to informal negotiations, formal restructuring offers the advantage of making it possible to adopt restructurings even when not all unsecured creditors have consented. A comparative disadvantage of formal restructuring is the mandatory appointment of a restructuring professional and a creditor committee, along with the resulting restrictions on the company's business operations during the proceedings.[26]

Insofar as a company finds it necessary to restructure secured debts, formal restructuring proceedings offer no particular advantages regarding consent requirements. This is because, as noted in Section 2.1, formal restructuring proceedings cannot affect secured claims without the secured creditor's consent.

There may, however, be instances where it is possible to achieve an out-of-court restructuring despite the opposition of some creditors whose debts the company seeks to restructure. This is because the company and its creditors may have made use of the option for creditors to waive *ex ante* the requirement that each creditor must consent to changes to its rights against the debtor. Contractual practice in the Norwegian bond market demonstrates this approach. The bond terms employed by Nordic Trustee, which acts as bond trustee for most bond issuances in the Norwegian market, permit amendments to bond terms without the consent of all bondholders.[27] Typically, approval from bondholders representing two-thirds of the outstanding bonds (excluding those held by the issuer) suffices for proposed amendments.[28] This applies to all types of changes, including reductions of

25 Viggo Hagstrøm, *Obligasjonsrett* (Herman Bruserud and others (eds), 3rd edn, Universitetsforlaget 2021) 907.

26 See *rekonstruksjonsloven* § 15.

27 See Clause 15.1(a) of the Norwegian Corporate Bond Terms template, available at <https://nordictrustee.com/service/documentation-and-templates/> accessed 30 October 2024 (hereinafter 'the NT Corporate Bonds Template').

28 NT Corporate Bonds Template Clause 15.1(g).

the principal amount and extensions of payment deadlines.[29] As a result, bond restructuring does not require unanimous consent from bondholders.

This feature of the bond terms has two notable implications. First, it allows for the restructuring of secured bond debt without the consent of all bondholders. This is an option that the formal restructuring framework does not provide, as secured claims are excluded from those subject to modification through non-consensual restructuring. Secondly, the voting clause in the bond terms makes the out-of-court restructuring of bond debts easier than would otherwise follow from the general principles of the law of obligations. This reduces the practical utility of formal restructuring proceedings in cases where a company's primary need is to restructure bond debt.

In sum, there is reason to believe that there will be cases where a company seeking to restructure bond debts will deem the costs associated with formal restructuring proceedings to outweigh the benefits and will instead opt for an out-of-court restructuring. Does actual restructuring practice support this hypothesis? While there are no comprehensive data on the number of out-of-court restructurings per year, it is possible to gain insight into the prevalence of such restructurings among companies with listed shares or bonds on markets operated by Oslo Børs (the Oslo Stock Exchange). These companies are subject to disclosure requirements, and disclosures are published on www.newsweb.no, a site operated by Oslo Børs.

Searches conducted on newsweb.no identified at least ten instances of companies with their centre of main interests in Norway–and therefore subject to Norwegian insolvency jurisdiction[30]–having made announcements during the period 2020–2023 regarding out-of-court restructurings involving externally held debts (i.e., excluding debt restructurings limited to shareholder loans). Over the same period, three such companies entered insolvent winding-up proceedings, while three initiated formal restructuring proceedings. These data are consistent with the analysis suggesting that formal restructuring proceedings often do not offer distinct advantages for a company seeking solely to restructure debts related to a single bond issuance.

29 This is expressly made clear by NT Corporate Bonds Template Clause 15.1(a).

30 *Konkursloven* § 146.

3.3. Restructuring through going-concern sales from insolvency estates

This section considers the advantages and disadvantages of formal restructuring proceedings compared to initiating insolvent winding-up proceedings and purchasing assets from the insolvency estate with the intention of continuing the company's business. The comparison focuses on a formal restructuring proceeding being used to reduce or reschedule a company's debt obligations versus a winding-up proceeding involving the transfer of assets to a newly formed company.

Unlike insolvent winding-up proceedings, formal restructuring proceedings enable the continued existence of a distressed company, thereby preserving the company's legal rights and privileges. By contrast, the insolvency estate may only seize and sell assets that are transferable or otherwise capable of being converted into money. Not all rights and privileges meet this criterion. Consequently, restructuring proceedings may preserve value associated with rights or privileges that an insolvency estate cannot seize and sell, whereas an insolvent winding-up proceeding cannot preserve such value. This may include public authorisations or contracts containing favourable terms for the company.

Another potential advantage of formal restructuring proceedings is that debt restructuring does not necessitate cash payments from the owner-manager. If the debt reduction is sufficient to secure the company's future payment capacity, there may be no need for shareholders to inject cash into the company. By contrast, liquidity is essential when purchasing assets from the insolvency estate to continue the business under a newly formed entity. A purchaser must have funds to pay the insolvency estate for the assets acquired. Therefore, there may be situations in which a liquidity-constrained owner-manager would favour formal restructuring proceedings over acquiring assets following an insolvent winding-up.

A disadvantage of a formal restructuring proceeding is that it requires the consent of at least some of the unsecured creditors. As noted in Section 2.1, a consensual restructuring requires unanimity, while a non-consensual restructuring requires approval from at least half of the unsecured creditors entitled to vote on the restructuring. Creditors must therefore agree to forgo their rights against the company. To persuade creditors to do so,

the company must provide information demonstrating that a debt restructuring is in their best interests. Supplying such data imposes costs on the company. Even if the company provides the necessary information, creditors will still incur costs in assessing it. If an individual creditor considers the assessment costs disproportionately high relative to the value of their claim, that creditor may choose neither to assess the information nor to vote. This could make it difficult for the company to obtain sufficient number of votes.

Conversely, purchasing assets from the insolvency estate in principle only requires an agreement with the insolvency professional managing the estate. There is nothing to prevent the insolvency estate from selling assets to a person who was a shareholder or otherwise connected to the company before the winding-up proceedings.[31]

Another potential comparative disadvantage of restructuring proceedings is that certain labour law rights are relaxed when an insolvency estate sells the insolvent company's assets.[32] Normally, a purchaser acquiring assets constituting a business assumes the seller's obligations towards employees engaged in that business.[33] Moreover, the purchaser is not permitted to invoke the acquisition as grounds for dismissal.[34] However, these rules do not apply when an insolvency estate sells a business.[35] In such cases, the purchaser does not automatically assume any contractual relationships with employees they do not wish to continue. By contrast, the commencement of restructuring proceedings does not per se affect employee rights. The formal restructuring proceeding does therefore not offer a means for restructuring a company's work force.

31 See Section 2.1.

32 See, generally, Alexander Sønderland Skjønberg, Eirik Hognestad and Marianne Jenum Hotvedt, *Arbeidsrett* (4th edn, Gyldendal 2024) 579–80.

33 *Arbeidsmiljøloven* § 16-2.

34 *Arbeidsmiljøloven* § 16-4.

35 *Arbeidsmiljøloven* § 16-1(2).

4. Conclusion

The background to this article is the low number of Norwegian companies making use of the Norwegian formal restructuring framework. We have examined whether there is reason to believe that financially distressed companies – i.e., companies whose businesses are viable – rely on alternative means rather than formal restructuring proceedings to ensure the continuation of their businesses. To this end, we considered the circumstances under which a company controlled by an owner-manager would prefer out-of-court restructuring or petitioning for insolvent winding-up proceedings, followed by purchasing assets from the insolvency estate with a view to continuing the business in a new legal entity. The analysis suggests that a company seeking to restructure debts arising from a single bond issue will often prefer an out-of-court restructuring over formal restructuring proceedings if the bond terms conform to the standards commonly used in the Norwegian bond market. Formal restructuring proceedings have both advantages and disadvantages compared to insolvent winding-up proceedings followed by an asset purchase from the insolvency estate to continue the business of a financially distressed company. The preferable option will depend on the specific circumstances of each case. Factors favouring formal restructuring include the business's reliance on legal rights and privileges that an insolvency estate cannot seize and sell, as well as liquidity constraints on the part of a potential purchaser. Factors favouring an insolvent winding-up include the presence of creditors with small claims and a desire to terminate employment relationships that cannot easily be severed under the general rules of Norwegian labour law.